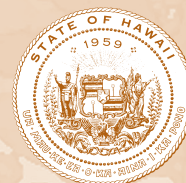


Holomua



Employees' Retirement System
of the State of Hawaii
Working to fulfill your retirement dreams...



2013 Legislative Update

The 2013 Hawaii State Legislature passed three bills related to the ERS and all three were signed by into law by Governor Abercrombie. Summaries of the legislation are noted below. For more information on these and other legislation, you may visit the State Capitol website at www.capitol.hawaii.gov.

Act 124 (H.B. 805): Relating to Federal Tax Qualification of the Employees' Retirement System - Effective: June 14, 2013

The ERS is a tax-exempt, qualified retirement plan under section 401(a) of the Internal Revenue Code (IRC). Compliance with the requirements of the IRC allows for favorable tax treatment of member contributions and does not require members to pay federal income taxes on the present value of their accrued vested benefits. In order for the System to retain its tax-qualified status, this Act proposes two mandatory amendments: (1) to reinforce the benefit limitations imposed by the Internal Revenue Code, and (2) to clarify vesting rules for the accrued retirement benefits for ERS members. Both amendments are technical clarifications to the existing ERS statutes and do not change requirements or benefits provided by the ERS.

Act 123 (H.B. 808): Relating to the Employees' Retirement System and Civil Unions - Effective: June 14, 2013

In order to maintain its tax-qualified status (see Act above), the ERS must comply with certain federal tax law requirements that specify when civil union partners are not considered "spouses" under federal law. This Act amends three areas: (1) the right to a 100% joint survivor benefit when a civil union partner beneficiary is more than a specified number of years younger than the retiree, (2) the right to defer death benefits, and (3) preferential rollover rights for lump sum payments. Civil union partners would still have the rights accorded to spouses under the portions of the ERS statutes that are not restricted by the IRS Code. This Act also adds a new section to ERS chapter 88 to confirm that marital and spousal terms are inclusive of civil unions and civil union partners, unless to do so would jeopardize the tax-qualified status of the ERS. (Note: Due to the June 26, 2013 U.S. Supreme Court ruling on the Defense of Marriage Act, portions of this summary may be dated.)

Act 124 (S.B. 1036): Relating to Employees' Retirement System Personnel - Effective: July 1, 2013

As successful investment of the ERS fund is one of the foundations to the longevity and stability of the system, this Act allows the ERS Board of Trustees, through its administrator, to appoint investment officers for the ERS investment office. The ERS currently has over \$12 billion in assets and an unfunded liability of \$8.4 billion. The investment office and new investment officers would assist and advise the ERS Board with critical information needed to structure the ERS investment portfolio to meet its asset goals and reduce the System's unfunded liability. Also, to be consistent with other government agencies and public pension plans, this Act changes the title of the ERS "Administrator" to "Executive Director".

Upon revision of Chapter 88, Hawaii Revised Statutes, due to this new legislation, updated sections will be available on our website at <http://ers.ehawaii.gov>. For specific questions on current legislation, you may call our office at (808) 586-1735.

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Wes' Corner



The 2013 Legislative session is over and the ERS initiated bills have passed (with one exception). As a result of the budget bill passing, we are now able to increase our Investment Office from 3 to 6 investment professionals. Although it will take some time to establish and recruit for the 3 additional positions, we are excited that our Investment Office will have more resources to oversee the \$12 billion-plus ERS investment portfolio. (It is interesting to note that public pension funds of our size usually have about 8 – 12 investment professionals.) The other bills that passed were to comply with the Internal Revenue Code and protect the ERS's tax-exempt status that affords favorable tax treatments for ERS members.

We are hopeful that the investment markets will continue to move positively. So far the first 5 months of 2013 have given us a return of about 8%. If this continues, the ERS should report double-digit investment returns for the 2013 fiscal year, which will have a positive impact on the ERS unfunded liability as of June 30, 2013.

Our schedule for filing sessions throughout the rest of the 2013 calendar year is on the ERS website. For those who are planning to file for retirement in the second half of this calendar year, please make sure to attend one of our filing sessions. We also encourage you to visit our website and read all the material pertinent to your retirement. Anyone considering other employment outside of State and county government should visit our website and contact us before making a decision. It's important that you know what you may be giving up should you decide to leave State or county government.

We should have more information in our next newsletter on any changes at the ERS. Until then, I hope that you are having a healthy and happy 2013.

Aloha,
Wes Machida

City Financial Tower - ERS Renovation and Building Investment

The main ERS office is located on the 14th floor of the City Financial Tower (CFT) at 201 Merchant Street. As many of you are aware the CFT is one of the real estate investments of the ERS as part of its diversified investment portfolio. However, since Suite 1400 was not large enough to accommodate the full ERS workforce comprised of Administration, Benefits, Accounting, Investments and Information Technology staff as well as the System's dedicated computer equipment, we also occupied parts of the 9th and 16th floors over the past few years.

We and our property managers found that there was much more interest in leasing the 9th and 16th floors of the CFT than the long-vacant 2nd and 12th floors. So in order to maximize this building's occupancy and its value as income property, the ERS made the decision to renovate and relocate our offices to take advantage of this opportunity. Floors were renovated to accommodate the ERS staff and systems from February through May 2013. Staff and equipment movement was completed at the beginning of June. We hope that you experienced little or no disruption in services during this period.

Suite 1400 on CFT's 14th floor will continue to be the ERS main office and all members and visitors should continue to report there for all ERS services.

New Option Factors for Pension Calculation

Effective January 1, 2014, the ERS will have new option factors for its pension calculation. These factors are used to calculate the Maximum Allowance-equivalent survivor and refund (if applicable) provision options available upon retirement. The Board of Trustees of the ERS adopted these new option factors as a result of the change in our investment rate assumption from 8% to 7.75% and changes in our membership's mortality assumptions.

These new option factors will affect members with membership dates prior to July 1, 2012 and who retire after December 31, 2013. More information on how this impacts your retirement options will be provided in our September Holomua newsletter which will be distributed to your Personnel Departments.

Report from Vijoy Chattergy, Chief Investment Officer

Aloha Kakou. In the last Holomua newsletter, I introduced the idea that the Investment Office operates like a factory that applies “earned experience” to “turn” information into high quality investment returns. If the analogy were true, we could be very pleased that recent strong performance is evidence of the “factory” operating at high capacity. Stock fund managers for the ERS have benefited from a mediocre but positive growth environment, while bond fund managers invested in securities that outperformed low interest rate government bonds that dominate the benchmark indexes. A couple of real estate managers sold properties in high demand, generating excess returns for the ERS. Brilliant interpretation of information led to positive absolute and relative returns. End of story.

Well, not exactly. In contrast to the production of many physical goods, the production of investment returns is highly suboptimal and entails interpretation, discounting, and elimination of vast amounts of raw materials (i.e., information) to create investment strategies and develop narratives to “explain” results. This is intended as a factual statement, not a value judgment. The information left on the “factory floor” is often contrarian, insightful, and compelling. If the primary investment thesis ends badly, the information left behind might be reassembled to provide an alternative explanation.

But why add this complication to the pristine concept of the Investment Office Factory? With current market conditions favorable, it is the perfect time to reaffirm the notion that with all the earned experience in the world, investment results may not turn out as expected. This uncertainty or variability around the returns produced by the Investment Office relates to the concept of “investment risk.”

Management of investment risks in the ERS portfolio is an important task of the Investment Office. Risk management is just as important as generating investment return. In fact, risk and return are very much two sides of a single coin. To target an expected return objective, we implicitly accept a level of risk. To accept risk (i.e., anything beyond hiding cash under the mattress), we implicitly anticipate some expected return.

Investment return is relatively simple to understand as a dollar or percentage change in value of assets from the previous period. However investment risk and investment risk management are concepts that are more complicated, nuanced, and varied. This is possibly the investment version of the *Anna Karenina* principle which famously starts Tolstoy’s novel, “Happy families are all alike; every unhappy family is unhappy in its own way.”

Unhappy Investment Office Factories define risk in a number of different ways, including permanent loss of capital, negative returns, returns below a benchmark, unexpected events, uncertainty (as in volatility or standard deviation), etc. Risks can also be differentiated as systematic and unsystematic. Systematic risks are risks that must be accepted, similar to how certain levels of air pollution are taken as given in an urban setting. Unsystematic risks pertain to particular sources that can be minimized, similar to how car exhaust pollution can be minimized through design and regulation. Additionally, the Investment Office should consider ERS plan-wide risks such as meeting pension obligations and unfunded liabilities.

Practically speaking, the ERS Investment Office must recognize risk management as the equal of return performance. Just as there is a return requirement, there should be target risk parameters, both at the portfolio level and with the individual fund managers and investments. Delineation of responsibilities for the identification and mitigation of risks should be established. Going forward, we expect to hire a full-time risk manager to work side-by-side with soon-to-be-hired investment analysts. As the shop floor of the Investment Office Factor begins to buzz with activity, everyone will be focused on the twin objectives of achieving long-term expected returns with acceptable levels of risks.



Retiring in 2013?

If you are planning to retire this year, you will need to make a counseling appointment with the ERS staff. At these appointments, the ERS staff will counsel you on your retirement process by assisting you with the completion of your retirement application and other required forms. Your retirement options will be explained and for that reason we encourage you to bring your spouse and/or significant other as well as your financial advisor, if applicable. You will receive a letter that provides you with estimated pension amounts as well as the option features available.

We also encourage you to attend a pre-retirement workshop prior to your scheduled counseling appointment. These workshops provide an overview on retirement and other areas related to your retirement planning. If you are interested, contact your department for the workshop schedule.

Once you determine your retirement date, our staff will guide you on the retirement process when you call to make a counseling appointment. The earlier you schedule your appointment the more it will help the ERS and your department to prepare for your retirement. Below is the upcoming filing session schedule for our members.

Oahu Members

If you plan to retire from September 1 to December 31, 2013 you may contact our office at (808) 586-1735 to schedule an appointment. Below are the upcoming dates for appointment times at 8 a.m., 9:15 a.m., 10:30 a.m., 1 p.m. and 2:15 p.m. at our ERS Office.

July 12, 19, 26, 31

August 2, 7, 9, 14, 15, 21, 23, 28, 30

September 4, 6, 11, 13, 18, 20, 27

October 3, 7, 8, 9, 10, 28, 29, 30, 31

November 1, 8, 13, 15, 20, 22, 25, 26, 27, 29

You may also visit our website at <http://ers.ehawaii.gov> for more information on the appointment schedule.

Hawaii, Kauai, Maui, Lanai, and Molokai

For our members on the neighbor islands, you may contact the ERS representative on your island to schedule a counseling appointment. Below are our representatives and phone numbers:

Hawaii: Rhoda Miyashiro at 974-4076 or Dayle Ishii at 974-4077

Kauai: Sheri Kunioka-Volz at 274-3011 or Paula Alquiza at 274-3010

Maui: Paul George at 984-8181 or Edward Paa at 984-8282

News from the EUTF

News from the Hawaii Employer-Union Health Benefits Trust Fund (EUTF)

- Open enrollment (OE) for active employees ended May 10, 2013. Changes made during OE will be effective July 1, 2013 and you should receive your new membership cards by July 1, 2013, if your enrollment form was submitted timely. You will only receive a new ID card if you are switching from HMSA to Kaiser or visa-versa, or enrolling in a plan for the first time. ChiroPlan Hawaii and VSP do not issue ID cards.
- If you do not receive your new membership cards by July 1, 2013 and you need to see a doctor or a dentist, or fill a prescription before you receive your new membership cards, send the EUTF an email at eutf@hawaii.gov. In the email subject line type: "URGENT CONFIRMATION OF COVERAGE NEEDED". The EUTF will review these emails as a priority and take steps to rush your enrollment. Please visit our website for more information at www.eutf.hawaii.gov.

Some helpful tips and information for employees who are considering retirement:

- The Retiree Reference Guide is posted on the EUTF website at www.eutf.hawaii.gov and provides valuable information on retiree plans, premiums, eligibility and Medicare.
- If you retire anytime during the year, other than January 1st, any dental and vision plan benefits you have utilized will be counted towards your retiree dental and vision plan maximums/limitations.
- If you are retiring and you or your dependent are 65 years or older, you and your dependent **must** enroll in Medicare Part B to be enrolled in the EUTF and HSTA VB retiree medical and/or prescription drug plans.
- Please contact the Social Security Administration (SSA) to begin your Medicare enrollment process approximately 3-months in advance of your retirement, by visiting their website at www.socialsecurity.gov or by calling them toll-free at 1-800-772-1213. Your Medicare effective date should be the same date as your retirement date.
- Once enrolled in Medicare Part B you are eligible to be reimbursed for your Medicare Part B premium. When you are ready to retire, call or stop by the EUTF for additional information.
- Be sure EUTF has your current address and phone numbers, by completing an EC-1 or EC-1H (enrollment form) and giving it to your personnel office. Your department personnel will forward your EC-1 or EC-1H form to the EUTF.

Important: The EUTF is a separate organization from the ERS. If you have any questions about information in this article, please **DO NOT** contact ERS. Please contact the EUTF directly at 586-7390 or toll-free at 1-800-295-0089, or email the EUTF at eutf@hawaii.gov. You can also visit our website for more information @ www.eutf.hawaii.gov.



Employees' Retirement System

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Scan the QR code with your smartphone
to directly access the ERS website.

Holomua

Active Members

April/May/June 2013

Ask ERS

Answers to some frequently asked questions:

Q: If I receive a pay increase effective July 1, 2013, how would the pay increase impact my pension if I retire on December 31, 2013?

A: The impact may be minimal as the increase in salary would probably be used for 6 months (July – December 2013) of 36 months for the average of your highest 3 years, assuming that these 6 months are included in your highest earnings to date.

Q: If I plan to retire at the end of 2014 and receive a retroactive lump sum pay increase in July 2013, would the payment be included in my pension calculation?

A: Probably, if the period of your salary increase is part of the highest earning periods for your HI-3 pension calculation. Your lump sum retroactive payment will be redistributed for the months that it should have been earned, not attributed to the month the payment was received. The HI-3 determination of your average salaries may include the redistributed salary period.

The "HI-3" is the average final compensation (AFC), which is the pay earned by a member during the three (3) highest 12 month periods of creditable service. The 12 month periods do not have to be a calendar or fiscal years; however, the 12 months must be consecutive.

Q: How long should I work at the higher salary for the pay increase to have a significant impact on my pension?

A: Remember that the AFC is based on an average of your highest 3 years. Therefore, earning three years of higher salaries would maximize your pension increase as it would be included in your HI-3 calculation provided that these are the highest earnings of your career.

How to Contact Us

Monday-Friday 7:45 a.m. - 4:30 p.m.
(except State holidays)

Oahu Office, Phone: (808) 586-1735

Kauai Office, Phone: (808) 274-3010

Hawaii Office, Phone: (808) 974-4077

Maui Office, Phone: (808) 984-8181

Molokai & Lanai, toll free to Oahu:
1-800-468-4644

Continental U.S. toll free to Oahu:
1-888-659-0708